



# Technical bulletin 2015/1 January to March



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# Foreword

Technical bulletins are prepared by Audit Scotland's Technical Services Unit (TSU), and approved by the Assistant Auditor General, to provide external auditors appointed by the Accounts Commission and Auditor General for Scotland with

- information on the main public sector technical developments in the quarter that are relevant to their audit appointment
- guidance from the TSU on any emerging risks identified in the quarter.

Technical bulletins are available to external auditors from Audit Scotland's *Technical reference library*, and published on the [Audit Scotland website](#) so that audited bodies and other stakeholders can access them.

It is important that auditors read this technical bulletin promptly so they are familiar with the information and guidance provided. The auditor action checklist section at the end of each chapter should be completed by a senior member of the audit team.

The articles on technical developments are intended to highlight the key points that the TSU considers external auditors require to be aware of. It may still be necessary for auditors to read the source material where greater detail is required. The documents referred to in the articles can be obtained by using the hyperlinks, where available. They are also available to external auditors from Audit Scotland's *Technical reference library*.

While auditors act independently, and are responsible for their own conclusions and opinions, the TSU has a role in ensuring that those conclusions and opinions are reached on the basis of informed judgement. Consistency in similar circumstances is important and **Audit Scotland's Code of audit practice therefore states that auditors should normally follow TSU guidance**. Auditors should advise the TSU promptly if they intend not to follow guidance provided in this technical bulletin on an emerging risk.

The TSU encourages feedback on this technical bulletin. Comments should be sent to [pobrien@audit-scotland.gov.uk](mailto:pobrien@audit-scotland.gov.uk).

More in-depth and extensive guidance is provided in separate technical guidance notes published by the TSU. Technical guidance notes published in the quarter are referred to in this technical bulletin, and can be obtained by using the hyperlinks to the [Audit Scotland website](#).

Audit Scotland makes no representation as to the completeness or accuracy of the contents of technical bulletins or that legal or technical guidance is correct. Points of law, in particular, can ultimately be decided only by the Courts. Audit Scotland accepts no responsibility for any loss or damage caused as a result of any person relying upon anything contained in a technical bulletin.

# Headlines

This chapter provides brief headlines for the articles on technical developments and guidance in this technical bulletin, classified by the audit year to which it relates, and referenced to the paragraphs containing the main article.

Local authority chapter	Paragraphs
<b>2014/15 audit year</b>	
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Recharges from the general fund to the HRA.	1 - 3
Application of the new accounts regulations to section 106 bodies.	4 - 7
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Local authority chapter	Paragraphs
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<b><i>Technical developments</i></b>	
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The Scottish Government has issued guidance on providing financial assurance for health and social care integration.	85 - 91
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The NAO has issued the 2014/15 disclosure checklists for charitable NDPBs and the annual report.	99 - 100
Treasury has issued the discount rate for post-employment benefits and general provisions at 31 March 2015.	120 - 124
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Central government chapter	Paragraphs
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SACDA has issued its 2014 report on consultants' distinction awards.	166 - 167
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Further education chapter		Paragraphs
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# Local authority chapter

## Introduction

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This chapter contains technical developments and guidance from the TSU on emerging risks in the quarter that are relevant to the local authority sector.

It should be read by external auditors with appointments in the local authority sector. Auditors should also read the cross-sectoral chapter.

## Guidance from the TSU on emerging risks

### HRA recharges

1. The TSU has received a number of enquiries from auditors regarding recharges from the general fund to the housing revenue account (HRA). Auditors are reminded of [technical bulletin 2014/1](#) (paragraph 94) which made reference to [Guidance on the operation of local authority HRAs in Scotland](#) issued by the Scottish Government.
2. The guidance identifies a number of key HRA operating principles including the need for a robust, written methodology for calculating and allocating costs to the HRA. The methodology should be in sufficient detail for tenants to understand why costs are being charged and who is benefiting from the services they relate to. This includes the allocation to the HRA of the appropriate proportion of trading operation surpluses attributable to council housing activities.
3. Auditors should refer to the Scottish Government guidance when considering a council's methodology for making recharges to the HRA.

### Application of the accounts regulations to section 106 bodies

4. [Technical bulletin 2014/3](#) (paragraph 21) advised auditors that [The Local Authority Accounts \(Scotland\) Regulations 2014](#) have been issued and provided a summary of the main provisions that apply from 2014/15. The article advised that the accounts regulations apply to all bodies covered by [section 106](#) of the *Local Government (Scotland) Act 1973*. The TSU has received a number of enquiries regarding how the regulations apply to these bodies in practice.
5. Section 106 states that the accounts regulations apply to joint committees, joint boards and regional transport partnerships in the same way as they do to a council, subject to any necessary modifications. Auditors should confirm that each body has considered the modifications that are necessary in their context, and have arrangements in place to comply with the regulations. This includes, for example, ensuring appropriate signatories to the accounts are identified and nominated, and that internal audit arrangements have been considered.

6. The accounts regulations also apply to local government pension scheme (LGPS) pension funds as statutory guidance requires that pension fund financial statements within the annual report should be considered an additional abstract of accounts which councils are required to prepare under section 96 of the 1973 Act.
7. Although the accounts regulations also apply to the trustees for any charity covered by section 106, Regulation 12 disappplies most of the provisions other than the inspection process for the accounts.

### **Audit of 2014/15 charity accounts**

8. Auditors will be aware that the TSU agreed with the Office of the Scottish Charity Regulator (OSCR) that an auditor's report was not required for 2013/14 statement of accounts where an application to wind up a charity had been submitted prior to 31 March 2014 (even if the charity remained on the charity register as at that date).
9. The TSU has been in discussions with OSCR over extending that arrangement to 2014/15. OSCR has agreed that an auditor's report is also not required for the 2014/15 statement of accounts for those charities where the application was submitted prior to 31 March 2014.
10. Where a charity is wound up (and hence removed from the charity register) during 2014/15, but the application was not made before 31 March 2014, the charity regulations require the submission of the statement of account to OSCR within 9 months of the date of removal. An auditor's report is required on these accounts as the transitional provisions allowed for 2013/14 do not apply. The financial year covered by the accounts would be the period from 1 April 2014 to the day on which the charity is removed from the register.
11. Auditors should
  - identify which charities were removed from the register since 1 April 2014
  - establish when the application for removal was submitted
  - where the application for removal was after 1 April 2014, audit the 2014/15 accounts for the appropriate period and provide an auditor's report to a timescale that allows the submission of the accounts and auditor's report within nine months of the date of removal.

### **Other emerging risks**

12. This chapter of the technical bulletin also provides guidance from the TSU on the following emerging risks
  - agency disclosures for pension fund accounts (see paragraph 63)
  - reports to audit committees on integration joint boards (see paragraph 88).

## Accounting developments

### Property, plant and equipment

#### Updated guidance on accounting for components

13. The [Chartered Institute of Public Finance and Accountancy](#) (CIPFA) has issued updated guidance on identifying and accounting for asset components. [LAAP bulletin 86 \(update\) Componentisation of property, plant and equipment under the IFRS-based code](#) addresses the requirements of the *Code of practice on local authority accounting in the UK* (the Code) that
  - each component of an item of property plant and equipment (PPE) with a cost that is significant in relation to the total cost of the item should be depreciated separately
  - where a component is replaced, the carrying amount of the old component should be derecognised to avoid double counting and the new component reflected in the carrying amount. Such recognition and derecognition takes place regardless of whether the replaced part has been depreciated separately.
14. The bulletin explains that components of PPE have different useful lives, may wear out at different rates or have different risks of impairment or obsolescence. It is therefore necessary to depreciate each significant component separately over its useful life in order that the comprehensive income and expenditure statement is fairly charged with the consumption of economic benefits of those assets.
15. It is essential that the principles for component accounting are established together with agreed and documented procedures which will facilitate this process. This should enable authorities to
  - identify significant components of their PPE
  - establish the value of such components and determine an appropriate depreciation charge which reflects the consumption of the economic benefit of the component.
16. The procedures should be communicated to all relevant staff and include a requirement to document assumptions and the basis on which estimates are made.
17. The stages set out in the bulletin for establishing procedures for component accounting are
  - establish appropriate de-minimis thresholds for items of PPE that can be disregarded. Once established, the threshold should be documented, used appropriately and applied consistently.
  - assess the materiality of items of PPE. This involves carrying out a review of the authority's PPE to identify those that are above the de-minimis level and therefore require consideration of whether they contain significant components.
  - set the principles to be used to determine which components of PPE above the de-minimis are significant. The principles need to specify the basis on which it will be determined whether the cost of a component is significant in relation to the overall asset.

They are likely to refer to the cost of the component as a proportion of the overall cost of the asset (including the new component) rather than an absolute amount. This bulletin has been updated to highlight that it is essential that the assessments are made as at the same date. This may mean

- estimating the current-day build cost of the asset and comparing the cost of the new component against that cost; or
- discounting back the cost of the new component to the date when the asset was initially recognised and comparing that adjusted cost against the original cost of the asset.
- attribute values of items of PPE to significant components. When an asset is separated into different components, authorities will need to consider whether the revaluation reserve balance for the asset should be allocated across the various components.

18. Auditors should refer to this guidance when considering whether authorities have identified and properly accounted for significant asset components.

## Service expenditure analysis

### Guidance on community safety expenditure

19. The [Local Authority \(Scotland\) Accounts Advisory Committee](#) has issued guidance on accounting for community safety expenditure and income from 2014/15. [Guidance on the classification of community safety expenditure](#) explains that local authorities provide a wide range of community safety services including
- crime reduction, e.g. fees paid to police forces to secure extra police officers for a particular area or providing crime prevention advice
  - community based CCTV cameras, i.e. those that do not fall within the definition of a specific service (e.g. cameras at a school should fall within the education service rather than community safety)
  - safety services, e.g. provision of safety railing.
20. From 2014/15, the guidance recommends that expenditure on community safety is to be classified within the service expenditure analysis as general fund housing (within the private sector housing renewal sub division).
21. Restatement of 2013/14 comparatives will be required where there is a material change in the classification of community safety expenditure and income.
22. This change in treatment excludes community safety expenditure that
- specifically benefits, and is to be funded by, HRA tenants
  - falls within the definition of any other specific service classification
  - impacts on the amount of expenditure or income previously recorded for trading standards or environmental health. This is to avoid it affecting grant aided expenditure

used to distribute government grant. Authorities are instead required to submit details of the impact to LASAAC and, if material, disclose it in their financial statements.

23. Auditors should refer to this guidance when considering whether authorities have properly accounted for community safety expenditure and income from 2014/15.

## Group financial statements

### Guidance on accounting for collaborations

24. CIPFA has issued guidance called *Accounting for collaboration in local government* which is intended to help local authorities review their collaborative arrangements and account appropriately for them in accordance with the new group accounting standards from 2014/15.
25. Collaborative arrangements take many forms and involve various parties, including other public bodies, voluntary organisations and commercial entities. The guidance examines the accounting consequences of collaborations in local government. Auditors should refer to this guidance when considering whether authorities have properly accounted for their collaborative arrangements.
26. The five main accounting outcomes that might arise from collaborative arrangements are as follows
- Preparation of group accounts including the relevant transactions and balances from an authority's interest in other entities in accordance with the adoption of the relevant standards by the 2014/15 Code. This is the case where the other entity meets the definition of a subsidiary, associate or joint venture.
  - Inclusion of transactions and balances relating to the arrangements in the authority's single-entity financial statements. This is the case where the arrangements meet the definition of a joint operation or recognition is required under other accounting standards.
  - Recognition of an investment in the authority's single-entity balance sheet. This is the case where the arrangements are a financial instrument for the authority.
  - Accounting for particular transactions with another party. This is the case where the relationship is with an independent other party, e.g. service provider.
  - No recognition is required as the arrangements do not involve the authority entering into any transactions or acquiring any rights that need to be accounted for.
27. Determining which outcome applies to a particular arrangement is sometimes straightforward, e.g. where an authority holds 100% of the shares in a company. In more complex circumstances, the arrangements may not involve a separate legal entity over which the authority's control/influence can be assessed and the determination might involve judgements about contractual terms.
28. The guidance provides a useful chart at paragraph 3.8 which illustrates a process for separating out these different considerations.

## Entities

29. Although it is a key element of the definition of a subsidiary, international financial reporting standards (IFRS) do not define precisely what is meant by the term 'entity'. The guidance offers the view that an entity would need to be capable of being treated legally like a person. However this is based on FRS 9 and is, in the TSU's view, inconsistent with the definition of entity in paragraph 9.1.2.25 of the Code which makes clear that use of the term is not limited to organisations that are corporate bodies in legal terms. Paragraph 397 of note for guidance 2014/11(LA) sets out the TSU's view that any committee or body to which section 106 of the 1973 Act applies should be considered an entity in this context.
30. The concept of structured entities can be relevant to any collaborative arrangement that operates through a separate entity. These entities are given prominence in the group accounts standards because of concerns that lack of information about off-balance sheet activities was a contributory factor to the global financial crisis. Consequently, focus is placed on arrangements where there is exposure to risk because an organisation has sought to secure control or influence over an entity through contractual arrangements while foregoing the traditional tool of voting power.
31. Structured entities are not subject to any special accounting treatment. However, the risk arising from an involvement in structured entities has been addressed by a requirement for specific disclosures for structured entities.

## Materiality

32. Having identified that the authority is the parent of a group for the purposes of the Code or needs to account for collaborative arrangements, the next consideration is whether the relevant modifications to the financial statements would make a material difference to their usefulness for users.
33. Paragraph 9.1.1.6 of the Code states that authorities with interests in subsidiaries, associates and/or joint ventures should prepare group accounts in addition to their single entity financial statements, unless their interest is not considered material. The Code discussion on materiality at paragraph 2.1.2.9 makes the following points
  - The focus of materiality is on the potential effect on the decisions or assessments of users of the accounts. Consideration of materiality therefore needs to take into account users and their interests.
  - Potential omissions need to be considered collectively as well as individually. It may be that none of the interests that an authority has in other entities are material individually, but cumulatively they are material.
  - It is not only the size of an item that is important, but also its nature. Qualitative factors can be as significant as quantitative factors.
34. Authorities should start from a presumption that the Code's provisions should be followed, until it can be established that a different approach does not risk a misreading of the

authority's overall financial position or performance that might be significant to users of the accounts.

35. The process that should be undertaken in assessing materiality is as follows

- An initial assessment of qualitative factors should be made to determine whether group accounts should be prepared, irrespective of the quantitative impact that consolidation might have on the authority's results and financial position. Authorities will need to consider the circumstances that surround their involvement in companies and other group entities and collaborative arrangements. For example, an authority will need to consider whether it depends significantly on these entities for the continued provision of its statutory services.
- If there are no definitive qualitative factors, authorities should consider quantitative matters and assess the likely impact of consolidation.
- If the quantitative assessment does not confirm absolutely that group accounts would be immaterial, authorities should revisit the qualitative factors to make sure that there are none that would decisively tip the balance of opinion away from producing group accounts.

### **Control**

36. Paragraph 8.2 of the guidance provides a useful diagram which lists the factors to be considered when determining control.

### **Group accounts**

37. The Code sets out the accounting treatment for group accounts and details the presentation and disclosure requirements.
38. Where group accounts are required, authorities are required to prepare accounts for the authority and for the group. However, these two separate sets of accounts can be presented alongside each other in a columnar approach. The guidance recommends side-by-side presentation of the financial statements, as it allows clearer comparison of the authority-only and the group financial results.
39. Chapter 13 contains two worked examples, one for line by line consolidation of a subsidiary and one on equity accounting for an associate.

### **Non-group arrangements**

40. The chart at paragraph 15.6 of the guidance shows how to categorise arrangements that do not fall into subsidiaries, associates or joint arrangements. For example it considers whether
- there are contractual arrangements to support the collaborative activity (if not, there are no accounting implications)
  - the contractual arrangements take the form of a financial instrument, and therefore should be accounted for as such



- the contractual arrangements give the authority rights or obligations that require to be recognised.
41. Even where there are no accounting implications, there may still be a requirement for disclosures where the arrangement is a structured entity.

### Guidance on transition to new standards

42. CIPFA has issued guidance on the transition to the new group accounting standards in 2014/15 in [LAAP bulletin 102 Accounting for collaboration-transition issues](#). The bulletin highlights that the revised definition of control in *IFRS 10 Consolidated financial statements* may result in new entities being brought within the scope of group accounts. As this would be the result of a change in accounting policy, this would normally require a full retrospective restatement.
43. Paragraph 9.1.2.66 of the Code sets out the steps to be taken for an entity that is to be consolidated that was not previously treated as a subsidiary. This involves measuring the assets, liabilities and minority interests in the entity on 1 April 2014 as if it had been consolidated from the date when the authority obtained control under the Code's requirements for IFRS 10
44. The Code however contains concessions that recognise practicable difficulties in potentially going back many years to calculate the prior period restatements. The concessions are based on restatements not being required where they are impracticable (i.e. an authority is unable to apply a requirement after making every reasonable effort to do so).
45. Paragraph 9.1.2.67 of the Code states that if measuring a subsidiary's assets, liabilities and minority interests is impracticable, an authority should use the beginning of the earliest period for which application is practicable as a deemed acquisition date. This means going back to the date when all of the following apply
- Information is available to allow the effects of retrospective application to be determined and measured reliably, without having to make unreasonable efforts to obtain that information.
  - There is no requirement in preparing figures to make assumptions about what management's intent was at the time.
  - it is possible when making significant estimates to separate out (without introducing subjective judgements) the information that provides evidence of circumstances that existed on the date that amounts are to be recognised and would have been available when the financial statements for that year were authorised for issue.
46. The bulletin also provides guidance on
- entities that would have been subsidiaries under the IFRS 10 test but control was lost before 1 April 2014
  - the steps to be taken for an entity that was consolidated in the group accounts prior to 2014/15 but does not meet the new definition of a subsidiary

- moving from proportionate consolidation to equity accounting for jointly controlled entities
  - adjustments needed where a jointly controlled entity becomes a joint operation so that the arrangement is no longer accounted for using the equity method
47. The bulletin also highlights that the only specific concession in relation to the Code's adoption of the requirements of *IFRS 12 Disclosure of interests in other entities* allows the new disclosures in relation to unconsolidated structured entities to be restricted to 2014/15 (i.e. no comparatives required for 2013/14).
48. Auditors should refer to this guidance when auditing the group financial statements in the 2014/15 annual accounts.

## Remuneration reports

### Amended regulations on elected members

49. The principal 2007 regulations that provide for the remuneration of elected members have been updated with effect from 1 April 2015.
50. [The Local Governance \(Scotland\) Act 2004 \(Remuneration and Severance Payments\) Amendment Regulations 2015](#) (SSI 7) substitute increased annual amounts for different categories of remuneration to members.

## Pension funds

### Note for guidance on auditing 2014/15 local authority pension fund annual accounts

51. The TSU has published [Note for guidance 2014/13\(LA\) Audit of 2014/15 local authority annual accounts \(pension funds\)](#) to provide auditors with guidance on planning and performing the audit of the 2014/15 LGPS pension fund annual accounts.
52. The note for guidance provides guidance on the areas that the TSU considers represent a generic risk of material misstatement in the 2014/15 financial statements to inform auditors' own risk assessments. The note also provides guidance on auditors' responsibilities to
- audit and express an opinion on elements of the remuneration report
  - express an opinion on the consistency of the management commentary with the financial statements
  - report on other matters such as the annual governance statement.
53. Auditors should use this note for guidance when planning and performing the audit of the 2014/15 LGPS annual accounts.

### 2014/15 example accounts and disclosure checklist

54. CIPFA has published guidance that illustrates the 2014/15 financial statements of LGPS pension funds. The publication also includes a disclosure checklist that identifies the Code's requirements in relation to pension funds. The 2014/15 *Local government pension scheme*

*example accounts and disclosure checklist* provides an example set of accounts that meet the minimum requirements of the Code.

55. It sets out a fund account and a net assets statement as well as information to be disclosed in the notes. Some key information required to be disclosed in the notes are discussed in the following paragraphs. Auditors should refer to this publication when auditing the 2014/15 LGPS pension fund financial statements.
56. The note on critical judgements in applying accounting policies (as required by Code paragraph 3.4.2.81) highlights the highly subjective nature of determining the fair value of private equity investments. It also explains the calculation of the pension fund liability and the fact that the estimate is subject to significant variances based on changes to the underlying assumptions.
57. The note on assumptions about the future and other sources of estimation uncertainty (as required by Code paragraphs 3.4.2.83 and 3.4.2.84) considers the items in the net assets statement for which there is a significant risk of material adjustment in the forthcoming year e.g. actuarial present value of promised retirement benefits, private equity and hedge funds.
58. The note of events after the reporting date (as required by Code paragraph 3.8.4.1) gives as an example of a non-adjusting event the marked decline in the global stock markets which would impact on the market value of the fund's investments were they to be valued as at the date the accounts were authorised for issue.
59. As a change from the previous edition, the note on management expenses follows the CIPFA guidance *Accounting for local government pension scheme management costs* (see [technical bulletin 2014/3](#) - paragraph 95) and analyses the costs of managing the fund between administrative costs, investment management expenses, and oversight and governance costs. It also separately discloses performance related fees and transaction costs.
60. The note on the nature and extent of risks arising from financial instruments (as required by Code paragraphs 7.4.3.1 to 7.4.3.10) provides illustrative wording for explaining market risk, credit risk and liquidity risk.
61. The note on related party transactions (as required by Code paragraph 6.5.5.1r) describes the relationship between the administering council and the pension fund, including the costs incurred and reimbursed in administering the fund and the amount paid as contributions. It also gives details of the members of the pension fund committee who are in receipt of pension benefits, and the employees of the administering council who hold key positions in the financial management of the fund.
62. The note on related party transactions follows Code paragraph 3.9.4.3 by stating that the disclosure requirements for key management personnel are satisfied by the disclosures for officer remuneration. However, as explained at paragraph 190 of note for guidance 2014/13(LA), this is based on the assumption that there are such disclosures in the same financial statements. The inclusion of a remuneration report in the authority's own financial

statements does not satisfy the disclosure requirements for key management personnel in the pension fund financial statements.

### **TSU guidance on agency disclosures**

63. Subsequent to the publication of the 2014/15 example accounts referred to at paragraph 54 (and note for guidance 2014/13[LA]), the TSU has been in discussion with CIPFA regarding the requirement to disclose an agency arrangement in respect of administering payments for 'added years'.
64. LGPS pension funds often administer added years payments as agents of employing authorities in respect of staff who have had their pension augmented under *The Local Government (Discretionary Payments and Injury Benefits) (Scotland) Regulations 1998*. Paragraph 3.4.4.1 of the Code requires authorities to disclose the nature and amount of any significant agency income or expenditure.
65. Although this disclosure is not included in the 2014/15 example accounts, CIPFA has indicated agreement with the TSU's views that disclosure of the agency arrangement for added years is required in 2014/15, and that the 2015/16 example accounts will be amended. It is the income and expenditure associated with running the payrolls that is relevant for disclosure purposes, rather than the payroll cash flows themselves.
66. Auditors should confirm that the 2014/15 LGPS pension fund financial statements disclose the agency arrangement in respect of administering payments for 'added years'.

### **Establishment of pension boards**

67. Regulations have been made which provide for the establishment of a pension board from 1 April 2015 for each authority that administers the LGPS. [The Local Government Pension Scheme \(Governance\) \(Scotland\) Regulations 2015](#) (SI 60) make each pension board responsible for assisting the administering authority secure compliance with
  - *The Local Government Pension Scheme (Scotland) Regulations 2014* (as explained in [technical bulletin 2014/2](#) - paragraph 198) and other legislation relating to the governance and administration of the LGPS
  - requirements imposed in relation to the LGPS by the Pensions Regulator.
68. A pension board is required to comprise four representatives appointed by scheme employers and four by relevant trade unions. The board may consider any matter concerning pensions it deems relevant to the activities of the relevant fund including
  - any reports produced for the pension committee
  - fund performance and administration
  - actuarial reports and valuations
  - funding strategy.

## Auditing developments

69. The [Accounts Commission](#) has issued a report based on the findings from local government audit work during 2014, including the audit of the annual accounts. [An overview of local government in Scotland 2015](#) was prepared by Audit Scotland and provides elected members with an independent view on how councils are managed and perform.
70. For example, the report highlights that councils had a total of £1.8 billion of useable reserves at 31 March 2014, which represents a decrease of 2% in 2013/14. General fund balances accounted for over half of this amount. Councils allocated most of their general fund balances (69%) for specific purposes, such as modernisation initiatives and local development projects. The remainder was unallocated and held as a contingency to help deal with unforeseen events such as rising interest rates, relieving the pressure on demand-led services, or other unplanned spending.
71. Councils need to consider both their level of reserves, and how they plan to use them, when developing financial plans and setting annual budgets. The proper officer is responsible for advising the council on the level of reserves it should hold and ensuring that there are clear procedures for keeping and using reserves. Auditors reported, however, that not all councils carried out a formal risk analysis to determine the appropriate level of reserves. Most councils had a policy to maintain unallocated general fund reserves at around 2 to 4% of their net spending on services.

## Other developments

### Housing benefits

#### 2014/15 subsidy claims

72. [The Department for Work and Pensions](#) (DWP) has issued *Notes on completion of form MPF720B - final subsidy claim 2014/15* and a letter relating to the completion of the housing benefit subsidy claim for 2014/15.
73. The deadlines for receipt of the
  - pre-certified claim to the DWP and external auditors is 30 April 2015
  - the certified claim by the DWP is 30 November 2015.

#### 2014/15 HB COUNT modules

74. [The Audit Commission](#) has issued the following modules of the 2014/15 HB COUNT approach
  - Module 2 contains a checklist to help auditors ensure that the authority's system is using the correct benefit parameters to calculate benefit entitlement and for the authority to claim the correct amount of subsidy.
  - Module 3 comprises workbooks to be completed for detailed testing, incorporating step-by-step guidance and a test result summary.

75. Module 1 has also been issued and provides an overview of the approach, but this is superseded in Scotland by guidance from the TSU.
76. For 2014/15, the key changes to HB COUNT are to reflect DWP changes to the regulations and subsidy order. The most significant of these are
  - from 3 March 2014 the removal of the spare room subsidy (RSRS) applies to pre 1 January 1996 cases
  - clarification of benefit cap exemptions for managed properties, refuges and hostels.
77. The Audit Commission has also developed an e-learning package setting out the principles of the HB COUNT approach to the certification of HB subsidy claims for 2014/15.

### Removal of the spare room subsidy

78. The DWP has issued [HB urgent bulletin U6/2014 Upper tribunal decisions CSH/41/14 and CSH/42/14](#) to provide details of decisions made by the Upper Tribunal relating to the determination as to whether a room is a bedroom for the purposes of the removal of the RSRS policy.
79. The Upper Tribunal found that the space standards set out in the *Housing (Scotland) Act 1987* are not determinative as to whether a room is a bedroom for the purposes of the RSRS policy in the social rented sector. The starting point for the determination is the landlord's description of the property. Local authorities should consider factors such as the size, configuration and overall dimensions of the room, as well as access, lighting, ventilation and privacy.
80. Rooms capable of being a bedroom should be classed as such, regardless of what it is actually being used for by the tenant.

### Guidance for NFI HB matches

81. The DWP issued a letter regarding the *National fraud initiative's* (NFI) housing benefit data matches in order to provide guidance to those authorities that have transferred responsibility for fraud investigations to the DWP.
82. All NFI housing benefit data matches will continue to be released to the relevant local authority. Authorities are then required to carry out an initial sift of the data matches to identify those which show potential fraudulent activity and refer them to the DWP.

### Miscellaneous

83. The DWP has issued the following circulars
  - [HB circular A18/2014 Housing benefit: Uprating 2015/16](#) and [HB circular A2/2015 War pensions: uprating 2015/16](#) to advise of the benefits rates from April 2015.
  - [HB circular A4/2015 Pension flexibilities](#) to advise how greater flexibility introduced to the pension system from 6 April 2015 will impact on housing benefit claims.

- [HB circular S11/2014 New burdens payment for real time information bulk data matching initiative](#) to announce funding to meet the costs of the *Real time information* bulk data matching initiative.
  - [HB circular S1/2015 Discretionary housing payments government contribution for 2015/16](#) confirming UK government funding for discretionary housing payments (DHPs) in 2015/16. There are no limits on DHP overall expenditure for Scottish local authorities.
84. [The Housing Benefit & Housing Benefit \(Persons who have attained the qualifying age for state pension credit\)\(Income from earnings\)\(Amendment\) Regulations 2015](#) (SI 6) have been issued to clarify how local authorities should calculate housing benefit claimants' income.

## Integration joint boards

### Guidance for integration financial assurance

85. The [Scottish Government](#) has issued guidance on providing financial assurance for health and social care integration. [Guidance for integration financial assurance](#) states that the assurance process should enable the integration authority (integration joint board [IJB] or lead agency) and the delegating local authority (and health board) to identify the resources to be delegated and the risks associated with the integrated functions.
86. The process should be proportionate to the potential risks involved and cover the whole transition period. It should be possible for partners to avoid some of the document reviews involved in a formal process of financial assurance by placing reliance on assurances from each other.
87. IJBs will not be able to formally participate in the financial assurance process until they are established during 2015/16. It is recommended that until then
- the shadow chief officer and chief financial officer should work with the local authority (and health board) in carrying out the assurance work
  - the shadow IJB should receive regular reports on the assurance work.
88. The guidance also recommends that the local authority (and health board) internal auditors should provide reports on the assurance process to the respective audit committees. In the TSU's view, the reports provided to the audit committee should be considered in the preparation of the 2014/15 governance statement. Where assurance reports have not been provided to the audit committee, this should be considered for inclusion within the governance statement. Auditors should confirm that is the case when reading the information in the 2014/15 governance statement.
89. The initial sums delegated to the IJB should be based on existing budgets, actual spend and the financial plans for delegated services. The budget should be assessed against the actual expenditure over the previous two to three year period and should include non-recurring funding and expenditure and savings and efficiency targets. Partners may find it helpful to treat the first year as a transitional year and agree to a risk sharing arrangement with allocations being adjusted in subsequent years.

90. There should be a post integration review undertaken by the respective audit committees and the results shared with the Scottish Government.

### Integration scheme regulations

91. Integration schemes are required by the *Public Bodies (Joint Working)(Scotland) Act 2014* to set out for each local authority area the agreed arrangements for joint working. The following regulations have been issued in respect of integration schemes
- [The Public Bodies \(Joint Working\) \(Scotland\) Act 2014 \(Prescribed Local Authority Functions, etc\) \(Scotland\) Regulations 2014](#) (SSI 345) sets out the prescribed functions to be delegated through an integration scheme. The functions can generally be described as adult social care services.
  - [The Public Bodies \(Joint Working\) \(Integration Scheme\)\(Scotland\) Regulations 2014](#) (SSI 341) prescribe the information to be included in an integration scheme. They require the information to include
    - governance arrangements, including the number of members and arrangements for the appointment of the chairperson
    - arrangements for the preparation of a strategic plan and overseeing operational delivery of integration functions
    - the process and timescale for the preparation of performance targets and improvement measures, and the reporting arrangements
    - the process to agree and amend payments to the integration authority and to deal with variances in spending on integration functions
    - the risk management strategy, arrangements for information sharing, dispute resolution and complaints handling.
92. Local authorities are required to have regard to the national health and wellbeing outcomes prescribed by [The Public Bodies \(Joint Working\) \(Scotland\) Act 2014 \(National Health and Wellbeing Outcomes\) \(Scotland\) Regulations 2014](#) (SSI 343) when preparing the integration scheme.

## Finance

### Changes to council tax reduction scheme

93. Changes have been made to the council tax reduction scheme. [The Council Tax Reduction \(Scotland\) Amendment Regulations 2015](#) (SSI 46)
- uprate figures that are used to calculate the amount of council tax reduction claimants are entitled to receive
  - amend the definition of 'couple' to take account of same sex marriages
  - extend the classes of persons who do not need to be habitually resident in the UK in order to qualify for a council tax reduction
  - amend the definition of persons who are not entitled to council tax reduction.



## Auditor action checklist

	Yes/No/N/A	Initials/date	W/P ref
1 Have you carried out the action recommended at paragraph 3 in respect of recharges to the HRA?			
2 Have you carried out the action recommended at paragraph 5 in respect of the application of the new accounts regulations to section 106 bodies?			
3 Have you carried out the action recommended at paragraph 11 in respect of the removal of charities from the register?			
4 Have you carried out the action recommended at paragraph 18 in respect of significant asset components?			
5 Have you carried out the action recommended at paragraph 23 in respect of community safety expenditure?			
6 Have you carried out the action recommended at paragraph 25 in respect of collaborative arrangements?			
7 Have you carried out the action recommended at paragraph 48 in respect of the transition to the new group accounts standards?			
8 Have you used the note for guidance referred to at paragraph 51 when planning and performing the audit of 2014/15 LGPS pension fund accounts?			
9 Have you carried out the action recommended at paragraph 55 in respect of the audit of 2014/15 LGPS pension fund accounts?			
10 Have you carried out the action recommended at paragraph 66 in respect of agency disclosures in 2014/15 LGPS pension fund accounts?			
11 Have you carried out the action recommended at paragraph 88 in respect of 2014/15 governance statements?			

## TSU contacts for local authority chapter

94. The contacts in the TSU for this chapter are

- Paul O'Brien, Senior Manager (Technical) - 0131 625 1795 or [pobrien@audit-scotland.gov.uk](mailto:pobrien@audit-scotland.gov.uk).
- Tim Bridle, Manager - Local Government (Technical) - 0131 625 1793 or [tbridle@audit-scotland.gov.uk](mailto:tbridle@audit-scotland.gov.uk).
- Anne Cairns, Manager – Benefits (Technical) - 0131 625 1926 or [acairns@audit-scotland.gov.uk](mailto:acairns@audit-scotland.gov.uk).

# Central government chapter

## Introduction

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This chapter contains technical developments and guidance from the TSU on emerging risks that are relevant to the central government sector.

It should be read by external auditors with appointments in the central government sector. It should also be read by auditors with appointments in the health sector and further education sector as most of the articles also apply to those sectors. Auditors should also read the cross-sectoral chapter.

## Guidance from the TSU on emerging risks

### Carry forward of grant in aid

95. The TSU is aware that a number of non-departmental public bodies (NDPBs) are reporting unspent grant in aid (GIA) for capital projects. The *Scottish public finance manual* (SPFM) [section on grant and GIA](#) states that unspent balances held at the end of the financial year are not liable to surrender to the Scottish Government. However, the Scottish Government may take back the GIA at the year end and make a new award of grant in the following financial year.
96. Auditors should confirm that NDPBs have discussed the treatment of any unspent GIA at 31 March 2015 with the Scottish Government and have accounted for it appropriately.

## Accounting developments

### General accounting

#### Amendments to 2014/15 FReM

97. [HM Treasury](#) has issued a revised version of the [2014/15 Government financial reporting manual](#) (the FReM). The main changes from the previous version are to section 6.2 in respect of *IFRS 7 Financial instruments disclosures*. Section 6.2 has been amended to
  - encourage bodies to make appropriate disclosures relating to significant credit risk arising from debtors
  - continue to require the disclosures on fair value measurements previously included at paragraphs 7.27 to 7.27B of IFRS 7. The requirements have been relocated to *IFRS 13 Fair value measurement* and (as explained at paragraph 102, that standard does not come into effect in the central government sector until 2015/16), the amendment to the FReM has been necessary to require the disclosures to be made in 2014/15.

98. Auditors should ensure they refer to amended 2014/15 FReM when auditing the 2014/15 annual report and accounts.

### 2014/15 disclosure checklists

99. The [National Audit Office](#) (NAO) has issued the [Disclosure checklist for 2014/15 charitable NDPBs](#) and the [Disclosure checklist for annual reports 2014/15](#) which are designed to ensure that bodies covered by the FReM have prepared their 2014/15 annual report and accounts in the appropriate form and have complied with all disclosure requirements. The guide is cross-referenced to the 2014/15 FReM, individual financial reporting standards, and the *Companies Act 2006*.
100. While the guide is designed primarily for the NAO's internal use, auditors in Scotland may also find it helpful. Auditors may wish to use the checklist when auditing the 2014/15 annual report and accounts. Auditors will need to generate a tailored checklist by selecting the criteria that applies to their audited body.

### 2015/16 FReM

101. Treasury has issued the [2015/16 FReM](#). The two significant changes from 2014/15 are
- the adoption of *IFRS 13 Fair value measurement*
  - restructuring the annual report.

#### Adoption of IFRS 13

102. IFRS 13 sets out requirements for assets measured at fair value and is applied in full by the FReM to
- assets that are not held for their service potential
  - operational assets which are surplus to requirements where there are no restrictions on disposal which would prevent access to the market.
103. IFRS 13 does not apply to operational assets which are in use delivering front line services or back office functions. Adaptations have been added to section 6.2 to reflect this approach. In addition, existing adaptations have been amended to refer to current value in existing use, rather than fair value, where IFRS 13 is not applied.
104. The guidance on property, plant and equipment has also been amended, particularly at paragraphs 7.1.4 to 7.1.8 and by the addition of a flowchart at paragraph 7.1.14. Paragraph 7.1.6 provides guidance on determining whether an asset is surplus. It clarifies that an asset is not surplus where there is a clear plan to bring it back into future use as an operational asset.
105. Similar changes have also been made to the adaptation for IAS 38 in respect of intangible assets, and the guidance on donated assets and heritage assets.
106. In addition, paragraph 7.1.14 has been amended to require disclosures if depreciated historical cost is used as a proxy for current value in existing use or fair value, including
- the classes of assets where it has been used

- the reasons why
- information about any significant estimation techniques.

### **Restructuring of annual report**

107. Chapter 5 has been extensively re-written to require the annual report and accounts to comprise
- a performance report
  - an accountability report
  - the financial statements.

### ***Performance report***

108. The performance report should provide information on the body, including its main objectives and strategies and the principal risks that it faces. The requirements are based on the matters the *Companies Act 2006* requires to be dealt with in a strategic report, but bodies are only required to follow the requirements to the extent they are incorporated at section 5.2 of the FReM.
109. The performance report is required to provide a fair, balanced and understandable analysis of the body's performance. It is required to have the following two sections
- The overview section should give a short summary that provides users with sufficient information to understand the organisation. The minimum requirements are set out at FReM paragraph 5.2.8 and include a performance summary.
  - The performance analysis section is for bodies to report on their most important performance measures. The minimum requirements are set out at FReM paragraph 5.2.10 and include a more detailed analysis and explanation of the development and performance of the body during the year.
110. The performance report should be signed and dated by the Accountable Officer or Chief Executive.

### ***Accountability report***

111. The requirements of the accountability report are based on the matters required by the *Companies Act 2006* to be dealt with in a directors' report and remuneration report but only need to be followed by bodies to the extent that they are incorporated into section 5.3 of the FReM.
112. The accountability report requires to be signed and dated by the Accountable Officer or Chief Executive. It should have sections for a
- corporate governance report
  - remuneration and staff report
  - parliamentary accountability and audit report.

### ***Corporate governance report***

113. The corporate governance report is required to explain the body's governance structures and how they support the achievement of its objectives. As a minimum, the corporate governance report must include the
- directors' report which should disclose the information listed at FReM paragraph 5.3.9, including the composition of the management board
  - statement of Accountable Officer's responsibilities, model examples of which are provided at Annex 1. Paragraphs 5.3.11 and 5.3.12 require the Accountable Officer to confirm that
    - there is no relevant audit information of which the external auditors are unaware, and that they have taken all the necessary steps to make themselves aware of any relevant audit information and to establish that the external auditors are aware of that information
    - the annual report and accounts as a whole is fair, balanced and understandable and that they take personal responsibility for the annual report and accounts and the judgments required for determining that it is fair, balanced and understandable.
  - governance statement prepared in accordance with Scottish Government guidance.

### ***Remuneration and staff report***

114. The required disclosures for the remuneration and staff report are set out at FReM paragraphs 5.3.15 to 5.3.27. This includes disclosure of
- the policy on the remuneration of directors for the current and future years
  - each component (e.g. salary, allowances, accrued pension benefit) and the overall single total remuneration figure for each director using the format and methodology set out by the Cabinet Office in the relevant employer pension notice
  - pension entitlements for each director in the format set out in the relevant employer pension notice
  - payment for compensation on early retirement or for loss of office
  - payments to past directors
  - the ratio between the median staff remuneration and the mid-point of the banded remuneration of the highest paid director.
115. The requirements for the staff report are set out at FReM paragraph 5.3.27 and include
- an analysis of staff numbers
  - an analysis of the number of persons of each sex who were directors, senior civil servants and employees
  - sickness absence data
  - off-payroll engagements and expenditure on consultancy
  - summary data on the use of agreed exit packages.

**Parliamentary accountability and audit report**

116. The parliamentary accountability and audit report is required to comprise information on
- regularity of expenditure
  - fees and charges
  - remote contingent liabilities
  - long-term expenditure trends.
117. The FReM also requires it to comprise the certificate and report of the Comptroller and Auditor General. In Scotland, this is the independent auditor's report.

**Other changes**

118. Other changes include the following
- Paragraph 1.2.1 c) now states that additional commentary on items may be provided in the accounting policy note or next to an individual disclosure note.
  - Paragraph 1.4.2 has been amended to reflect the introduction of two new charities SORPs.
119. Paragraph 2.2.7 has been added to state that the Accountable Officer should not approve the accounts unless they are satisfied that the accounts give a true and fair view.

**Provisions****2014/15 discount rate**

120. HM Treasury has issued [PES\(2014\)9](#) to announce the discount rate for post-employment benefits liabilities and general provisions as at 31 March 2015.
121. The discount rate for post-employment benefits and early departure provisions will change from 1.8 % real to 1.3% real from 31 March 2015. The financial assumptions, based on market conditions, related to post employment benefit discount rates are set out in an annex. Funded schemes within central government should use a discount rate based on financial assumptions at 31 March each year, rather than these assumptions which are as at 30 November.
122. The real discount rates to be applied to provisions recognised in accordance with IAS 37 as at 31 March 2015 are as follows:
- The short term rate (for cash-flows up to 5 years from the statement of financial position date) is minus 1.5%.
  - The medium term rate (between 5 and 10 years) is minus 1.05%.
  - The long term rate (more than 10 years) is unchanged at 2.20%.
123. The change in discount rates could result in non-cash negative annually managed expenditure (AME) arising from interest income. This income can only be used for expenditure relating to provisions, or for depreciation of capital assets that have been donated.

124. Auditors should refer to this announcement when auditing provisions in the 2014/15 annual report and accounts.

## Auditing developments

### Notes for guidance on auditing 2014/15 central government annual report and accounts

125. The TSU has published [Note for guidance 2015/1\(CG\) Audit of 2014/15 central government annual report and accounts](#) and [Note for guidance 2015/2\(CG\) Audit of 2014/15 central government annual report and accounts \(charitable NDPBs\)](#) to provide auditors with guidance on planning and performing the audit of the 2014/15 central government annual report and accounts.
126. The notes for guidance provide guidance on the areas that the TSU considers represent a generic risk of material misstatement in the 2014/15 financial statements to inform auditors' own risk assessments. The note also provides guidance on auditors' responsibilities to
- audit the regularity of expenditure and income
  - audit part of the remuneration report
  - consider the consistency of the management commentary/trustees' annual report with the financial statements
  - review other matters such as the governance statement and any summarised financial statements.
127. Auditors should use the appropriate note for guidance when planning and performing the audit of the 2014/15 central government annual report and accounts.

### 2014/15 Government Banking Service account information

128. The TSU will obtain information on account balances at 31 March 2015 for central government bodies and health boards from the Government Banking Service (GBS) and distribute them to relevant auditors. The GBS operates accounts with the Royal Bank of Scotland and Citibank.
129. The GBS has confirmed that the arrangements for 2014/15 are unchanged, and therefore they will require bodies with new GBS accounts to submit an *Auditor authorisation form* to allow disclosure of account balances to auditors.
130. Auditors should confirm the account details at their bodies have not changed from 2013/14 and that, where required, their bodies have submitted an *Auditor authorisation form* to the GBS.



## Auditor action checklist

	Yes/No/N/A	Initials/date	W/P ref
1 Have you carried out the action recommended at paragraph 96 in respect of unspent GIA at the year?			
2 Have you carried out the action recommended at paragraph 98 in respect of the 2014/15 FReM?			
3 Have you considered the action suggested at paragraph 100 in respect of the disclosure checklists?			
4 Have you carried out the action recommended at paragraph 124 in respect of changes to the discount rate for provisions?			
5 Have you used the appropriate note for guidance referred to at paragraph 125 when planning and performing the audit of the 2014/15 central government annual report and accounts?			
6 Have you carried out the actions requested at paragraph 130 in respect of the GBS account information?			

## TSU contacts for central government chapter

131. The contacts in the TSU for this chapter are

- Neil Cameron, Manager - Central Government and Health (Technical) - 0131 625 1797 or [ncameron@audit-scotland.gov.uk](mailto:ncameron@audit-scotland.gov.uk).
- Helen Cobb, Technical Adviser (Central Government, Health and Further Education) - 0131 625 1901 or [hcobb@audit-scotland.gov.uk](mailto:hcobb@audit-scotland.gov.uk).

# Health chapter

## Introduction

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This chapter contains technical developments and guidance from the TSU on emerging risks in the quarter that affect the health sector.

It should be read by external auditors with appointments in the health sector. Auditors should also read the central government chapter and cross-sectoral chapter.

## Guidance from TSU on emerging risks

### Governance requirements for social care integration

132. The guidance from the TSU at paragraph 88 in the local authority chapter on reporting to audit committees in respect of integration joint boards also applies to the health sector.

## Accounting developments

### General accounting

#### 2014/15 accounts manual

133. The [Scottish Government Health and Social Care Directorates](#) (SGHSCD) has issued the *2014/15 NHS board accounts manual for the annual report and accounts* (the accounts manual) to interpret the accounting guidance contained in the FReM for the NHS in Scotland.

134. Auditors should refer to the accounts manual when auditing the 2014/15 annual report and accounts.

135. The terminology throughout the accounts manual has been amended to make it consistent with the FReM. For example, the full title of the manual has been amended to refer to the annual report rather than the directors' report. The main changes to the accounts manual from 2013/14 are in respect of the

- foreword, which are aimed at improving the quality of the published annual accounts
- management commentary and remuneration report, which reflect guidance issued for 2013/14.

#### Foreword

136. A paragraph has been added to page 5 of the accounts manual to remind boards that the annual report and accounts should be prepared to the highest standards and presented in a way that is helpful and informative to the user.

137. It also states that, although the consolidation template may be used as a basis for preparing their published annual accounts, it should be tailored to suit the individual board's

circumstances. Disclosure is not required if an item is not material or does not apply to the board's circumstances.

138. Clarification has been added that, although the manual covers Scottish financial returns (SFRs) which are required to be submitted to the SGHSCD, SFRs should not be included in the published annual report and accounts.

### **Management commentary**

139. The operating and financial review has been retitled the management commentary, which now comprises a directors' report and a strategic report. The 2014/15 accounts manual has been updated to reflect guidance which advised boards of changes to the FReM in respect of the directors' report and strategic report which applied from 2013/14 but which had not been reflected in the 2013/14 accounts manual.

### **Strategic report**

140. Pages 8 to 11 of the manual set out the disclosures for the strategic report. These include the following
- A brief history of the board and its statutory background.
  - The main trends and factors likely to affect the future development, performance and position of the board.
  - An analysis using financial and key performance indicators.
  - Sustainability reporting requirements.
  - Information on social, community and human rights policies.
  - A description of the strategy and business model.
  - A breakdown showing the number of persons of each gender who were directors, senior managers and employees of the board as at the end of the financial year.
141. Some disclosures previously included under the directors' report, including a note that the accounts have been prepared under an accounts direction, have been moved to the strategic report.

### **Directors' report**

142. Pages 12 to 14 of the manual set out the disclosures for the directors' report. Changes from the 2013/14 manual include the requirements for disclosure of
- sickness absence data
  - published personal data related incidents
  - how often members attended board meetings.
143. The wording under the heading 'date of issue' at paragraph 8 has been amended to clarify that this refers to the date that the board approved the financial statements. The Chief Executive is still required to sign the directors' report on the date the annual report and accounts are authorised for issue.

### Remuneration report

144. The guidance on page 18 regarding the remuneration report has been updated to reflect the guidance issued by the SGHSCD in 2013/14 on the requirement to disclose the single total remuneration figure for each director.
145. The single total remuneration figure should include (in addition to salary, performance related pay and benefits in kind) pension benefits accrued during the year. This should be calculated as
- the real increase in pension multiplied by 20
  - plus the real increase in any lump sum
  - less the contributions made by the individual.
146. The real increase excludes increases due to inflation or any increase or decrease due to a transfer of pension rights.
147. The definition of remuneration has also been amended to remove employers superannuation and other pension contributions.

### Other changes

148. Other changes include the following
- The guidance on page 24 includes a table setting out which sections of the annual report and accounts should be signed and by whom.
  - Page 104 has been updated to reflect that the discount rate for post-employment benefits set out in PES(2014)9 (referred to at paragraph 120).
  - A table has been added to the timetable section to clarify the required number of paper and electronic copies of the annual report and accounts, e.g. Audit Scotland requires two signed copies.

### 2014/15 capital accounting manual

149. The SGHSCD have issued the *2014/15 NHS capital accounting manual* to interpret the accounting guidance contained in the 2014/15 FReM on capital accounting issues in the NHS. The main changes from the previous version are as follows
- Chapter 6 has been updated to include the loss or damage to assets in the normal course of business in the list of impairments that can be funded by non-cash departmental expenditure limits. The normal course of business includes all loss or damage resulting from management or staff action or inaction, including theft.
  - Chapter 12 has been amended to reflect the FReM guidance that service concession arrangement infrastructure assets should be recognised when the IAS 16 recognition criteria are met.
  - Guidance has been added to chapter 12 setting out the arrangements for the payment of design fees for hub projects, i.e.

- For capital funded projects, existing capital resource limit (CRL) funding should be used.
- For revenue funded projects, the board should request additional CRL from SGHSCD to provide a repayable loan to the hubco (i.e. the joint venture company that is developing and delivering community infrastructure projects).

150. Auditors should refer to the accounts manual when auditing the 2014/15 annual report and accounts.

## Provisions

### Guidance on clinical negligence claims from 2014/15

151. The SGHSCD has issued guidance on the revised accounting treatment and presentation of the *Clinical negligence and other risks indemnity scheme* (CNORIS) from 2014/15. *Guidance on accounting for clinical negligence and other risks indemnity scheme* explains that CNORIS is a mechanism for pooling risk in respect of legal claims related to clinical negligence. Boards contribute to the CNORIS pool each financial year at a pre-agreed contribution rate based on their associated risks. If a claim is settled, the board is reimbursed for the value of the settlement less a £25k 'excess' fee.
152. When a legal claim is made against a board, it assesses whether a provision requires to be recognised based on information provided by the Central Legal Office. If a provision is required, the board also recognises an associated debtor to reflect reimbursement from the scheme. This provision and associated debtor have been recognised in previous years and continue to be required.
153. From 2014/15, boards are also required to recognise a second provision for their contributions to the scheme in future years. This means there should be two related, but distinct, provisions recognised as a result of participation in the scheme. The second provision will be funded from AME budget cover.
154. The second provision should have been recognised in previous years and therefore a prior year restatement is required. The Scottish Government will provide the figures required for this restatement.
155. The guidance provides wording at Appendix A for a disclosure note that should be included in the financial statements. This takes the various CNORIS-related disclosures in the statements and includes them in one note to provide a comprehensive explanation of how CNORIS works.
156. Auditors should refer to this guidance when auditing the CNORIS provision in the 2014/15 annual report and accounts.. Auditors should ensure boards consider the nature, as well as the amount, of the transaction when considering materiality.

## Auditing developments

### Notes for guidance on auditing 2014/15 health annual report and accounts

157. The TSU has published [Note for guidance 2015/3\(H\) Audit of 2014/15 health annual report and accounts](#) to provide auditors with guidance on planning and performing the audit of the 2014/15 health annual report and accounts.
158. The note for guidance provides guidance on the areas that the TSU considers represent a generic risk of material misstatement in the 2014/15 financial statements to inform auditors' own risk assessments. The note also provides guidance on auditors' responsibilities to
- audit the regularity of expenditure and income
  - audit part of the remuneration report
  - consider the consistency of the management commentary with the financial statements
  - review other matters such as the governance statement, consolidation templates, and any summary financial information.
159. Auditors should use the note for guidance when planning and performing the audit of the 2014/15 health annual report and accounts.

## Corporate governance developments

### 2014/15 guidance on governance statements

160. The SGHSCD have issued *Guidance on governance statements 2014/15* to help Chief Executives prepare their board's governance statement. The Chief Executive is responsible for reviewing the adequacy and effectiveness of the system of internal control. The review should comprise an assessment of the effectiveness of overall corporate governance and risk management arrangements, and be supported by internal and independent assurances.
161. The governance statement should comply with guidance in the SPFM, be accurate and complete, and fairly report the known facts. It is for the Chief Executive to decide how to organise the governance statement but the guidance provides a suggested proforma. Features of the proforma that must be included in the statement are disclosures of
- the governance framework, including information on the committee structure
  - an assessment of the board's compliance with the SPFM, with explanations where a different approach has been adopted
  - details of the operation of the board
  - the board's assessment of its own performance. Boards may include a link to an online copy of their assessment rather than duplicating the details in the governance statement
  - an assessment of the board's risk management arrangements and risk profile
  - any significant control weaknesses. The guidance sets out factors to be considered when assessing significance. It requires boards to give specific consideration to any reports

from inspection agencies, and the board's performance in relation to treatment time guarantees.

162. As indicated at paragraph 88, in the TSU's view, governance issues around the assessment work carried out in preparation for health and social care integration should be considered for inclusion in the governance statement.
163. The audit committee has a specific responsibility for reviewing the disclosures included in the governance statement. It should consider the information it needs, which may include the supporting information provided to the Chief Executive.
164. A letter of assurance from the Chair of the audit committee is required to be sent to the Chair of the Scottish Government Health and Wellbeing Audit and Risk Committee to
  - provide assurances on the governance of the board
  - advise of any governance matters that require to be brought to the attention of the Scottish Government Audit Committee.
165. Auditors should refer to this guidance when reading the information in the 2014/15 governance statement.

## Other developments

### Pay and workforce planning

#### 2014 consultants' distinction awards

166. The Scottish Advisory Committee on Distinction Awards (SACDA) has published its [Annual report 2014](#) which sets out the results of the 2014 awards round for distinction awards to consultants in NHS Scotland.
167. The report includes a list of all distinction award holders as at 30 September 2014.

### Planning and performance management

#### 2015/16 local delivery plan guidance

168. The Scottish Government has issued [NHSScotland local delivery plans 2015/16](#) to provide guidance on the preparation of local delivery plans (LDPs) for 2015/16. Boards are to develop plans focused on strategic priority areas, including prevention, health inequalities, primary care, and integration.
169. Health and social care partners are required to take account of the health and social care outcomes set out in legislation (referred to at paragraph 92) when developing their plans. Once established, integration authorities will lead on the delivery of these outcomes.

## Social care integration

### Guidance on hospital set aside budgets

170. The Scottish Government has issued guidance on establishing the amount to be set aside by health boards for integrated health and social care services delivered in a large hospital. [Guidance on financial planning for large hospital services and hosted services](#) recommends that this should be determined by analysis of hospital activity and cost information.
171. Hospital patient administration systems should be used to identify the hospital activity and capacity used by patients for each integration authority. It is recommended that data used for the first strategic plan should be based on an average of the previous three years of activity. However, decisions on capacity and service redesign may result in subsequently result in different consumption patterns.
172. Performance against the plan for hospital capacity requires to be reported to allow the strategic plan to be adjusted and remedial action taken in year if necessary. Any adjustments to the set aside resource to reflect variances in performance should be made through annual adjustments to the strategic plan.
173. The methodology for costing this activity is a local decision, but a consistent methodology should be applied across all integration authorities in a health board area. The same methodology should be applied to hosted services provided in hospital.

### Other integration scheme regulations and guidance

174. Regulations and guidance relevant to social care integration are included at paragraphs 78 to 85 of the local authority chapter.
175. In addition, regulations have been issued which prescribe the health board functions to be delegated through an integration scheme. [The Public Bodies \(Joint Working\) \(Scotland\) Act 2014 \(Prescribed Health Board Functions\) \(Scotland\) Regulations 2014](#) (SSI 344) sets out
- the functions that may be delegated at Schedule 1
  - the functions that must be delegated at Schedule 2
  - the health board services related to these functions at Schedule 3.

## Auditor action checklist

	Yes/No/N/A	Initials/date	W/P ref
1 Have you carried out the action recommended at paragraph 134 in respect of the 2014/15 accounts manual?			
2 Have you carried out the action recommended at paragraph 150 in respect of the 2014/15 capital accounting manual?			



	Yes/No/N/A	Initials/date	W/P ref
3 Have you used the note for guidance referred to at paragraph 157 when planning and performing the audit of the 2014/15 health annual report and accounts?			
4 Have you carried out the action recommended at paragraph 165 in respect of 2014/15 guidance on governance statements?			
5 Have you carried out the actions requested at paragraph 130 in respect of the GBS account information?			

## TSU contacts for health chapter

176. The contacts in the TSU for this chapter are

- Neil Cameron, Manager - Central Government and Health (Technical) - 0131 625 1797 or [ncameron@audit-scotland.gov.uk](mailto:ncameron@audit-scotland.gov.uk).
- Helen Cobb, Technical Adviser (Central Government, Health and Further Education) - 0131 625 1901 or [hcobb@audit-scotland.gov.uk](mailto:hcobb@audit-scotland.gov.uk).

# Further education chapter

## Introduction

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This chapter contains technical developments and guidance on emerging risks in the quarter that are relevant to further education colleges.

It should be read by external auditors with appointments in the further education sector. Auditors should also read the central government chapter and the cross-sectoral chapter.

## Accounting developments

### Briefing note on review of resource returns

177. [Colleges Scotland](#) has issued a briefing note on proposals for external auditors to review the annual resource returns. The [Office of National Statistics reclassification briefing note on change of accounting year end](#) is intended to explain to board members, principals and other college senior managers the impact of moving the financial year end from 31 March to 31 July from 2014/15.
178. A key issue is that Scottish Government funding is still provided on a fiscal year basis, i.e. ending 31 March. The [Scottish Funding Council](#) (SFC) has proposed that the resource returns at 31 March (which are submitted to the SFC to monitor how funding was spent) should be reviewed by external auditors to provide assurance on the financial information contained in the returns.
179. The objective of the review engagement would be to enable an auditor to state whether anything has come to their attention that causes them to believe that the financial returns are not prepared in accordance with the applicable financial reporting framework (i.e. limited or 'negative' assurance). The TSU has agreed to arrange a review engagement in principle, subject to acceptance by the Scottish Government.
180. The TSU will provide guidance to auditors on performing and reporting on the review engagement in due course once the SFC has obtained confirmation from the Scottish Government that the approach is acceptable.

## Corporate governance developments

### New governance code

181. The SFC has issued a [Code of good governance for Scotland's colleges](#) which sets out standards of good governance for all college boards with effect from 1 August 2014. It has also issued an accompanying guidance note [Good practice in college governance](#) which advises that the code represents the SFC's view of good practice in governance.

182. It is therefore a condition of grant that colleges comply with the code. It is expected that regional strategic bodies (RSBs) will also follow the code, where relevant. Each college is required to report compliance with the code in its corporate governance statement. In addition, the chair is encouraged to report personally as to how the principles have been applied by the board.
183. The principles of the code are set out in five sections as follows
- Section A covers leadership and strategy including stating that the board is responsible for the college's strategic direction, and ensuring a performance measurement system is in place. For an assigned college, the board is required to have regard to the strategy determined by the RSB.
  - Section B covers the quality of the student experience.
  - Section C sets out the accountability requirements including the responsibilities of the board and committees.
  - Section D deals with effectiveness including the responsibilities of the board Chair, members and the principal to ensure the board operates effectively.
  - Section E deals with relationships and collaboration between colleges, RSBs, staff and students.
184. Where a college's practice is not consistent with any principle of the code, it is required to make this known immediately to the SFC or RSB. In the event of the latter, the RSB is required to provide the SFC with details. An explanation for the inconsistency requires to be clearly stated in the college's corporate governance statement. Colleges will be expected to offer a clear rationale for exceptions in the context of their operational model and to identify mitigations.
185. Auditors should use the code when reading the information in the 2014/15 corporate governance statement.

### New financial memorandum

186. The SFC has issued a new [Financial memorandum with fundable bodies in the college sector](#) which applies from 1 December 2014. It is a condition of the grants from the SFC that that colleges and RSBs comply with the requirements of the memorandum.
187. The memorandum is set out in four parts as follows
- Part 1 deals with the relationship between the SFC and institutions, and the responsibilities of each for the proper stewardship of public funds.
  - Part 2 imposes a number of general requirements on all institutions including the requirement to repay grant if a requirement is not complied with.
  - Part 3 applies additional requirements to RSBs, regional colleges and regional boards. Regional colleges and regional boards are required to follow the requirements of the SPFM except where special actions or agreed derogations are set out in the memorandum.

188. Auditors should confirm their colleges are aware of the memorandum and have arrangements in place to ensure they comply with it.

## Other developments

### Finance

#### Use of depreciation funding in 2014/15

189. The SFC has issued guidance on the release of 2014/15 funding, which was previously earmarked for depreciation, for other purposes. [Financial adjustments for student support and other purposes in financial year 2014/15](#) explains that prior to reclassification as central government bodies, colleges used available funds to cover depreciation charges on their fixed assets.
190. Following reclassification, colleges have been given a cash budget to cover their costs (including depreciation) and a separate budget for fixed assets. As depreciation is not a cash cost, there is additional budget available which can be used to meet other revenue expenditure, including student support.
191. As colleges are required to spend the full amount of their cash budgets, this additional revenue expenditure may result in an operational deficit in colleges' 2014/15 income and expenditure accounts equivalent to their net depreciation charges. The SFC will adjust for these deficits when assessing colleges' financial health.

## Auditor action checklist

	Yes/No/N/A	Initials/date	W/P ref
1 Have you carried out the action recommended at paragraph 185 in relation to the code of good governance?			
2 Have you carried out the action recommended at paragraph 188 in relation to the financial memorandum?			

## TSU contact for further education chapter

192. The contact in the TSU for this chapter is Helen Cobb, Technical Adviser (Central Government, Health and Further Education) - 0131 625 1901 or [hcobb@audit-scotland.gov.uk](mailto:hcobb@audit-scotland.gov.uk).

# Cross-sectoral chapter

## Introduction

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This chapter contains technical developments and guidance from the TSU on emerging risks in the quarter that are relevant to all sectors.

It should be read by all external auditors. Information on developments and guidance from the TSU in the quarter that are relevant to only one sector are covered in the relevant sector-specific chapter.

## Guidance from TSU on emerging risks

### Auditor's responsibilities for management commentary

- 193.** The TSU has received some enquiries from auditors regarding their responsibilities in respect of the management commentary included in the annual report and accounts. Auditors are required to read the management commentary and express an opinion in the auditor's report as to whether it is consistent with the financial statements.
- 194.** In this context, an inconsistency is anything in the management commentary that contradicts information contained in the audited financial statements. Inconsistencies include
- differences between amounts or narrative appearing in the financial statements and the management commentary
  - differences between the bases of preparation of related items where the figures are not directly comparable and the different bases are not disclosed
  - contradictions between figures in the financial statements and the narrative explanation of those figures in the management commentary.
- 195.** Auditors should also read the management commentary to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by auditors in the course of performing the audit. If revision of the management commentary is necessary, and the audited body refuses to make the revision, auditors should include in the auditor's report an 'other matter' paragraph describing the matter.
- 196.** Further guidance is included in the notes for guidance from the TSU on auditing the 2014/15 annual report and accounts. Auditors should read the management commentary and report in accordance with this guidance.

### Holiday pay and overtime

- 197.** A [recent ruling from the Employment Appeal Tribunal](#) states that compulsory overtime is part of an employee's normal remuneration and therefore should be included in the calculation of pay for holiday leave taken. The position on voluntary overtime is less clear.

198. Public bodies have not previously included overtime in their calculations of holiday pay owed to employees. Although this decision may yet be subject to appeal, auditors should confirm that audited bodies are considering whether the criteria for recognising a provision are met, including obtaining legal advice.

### New requirement to report to Pension Regulator

199. The TSU has identified that auditors of public service pension schemes are required to report certain breaches of the law to the Pension Regulator from 1 April 2015 under [section 70 of the Pensions Act 2004](#). The application of section 70 was extended to cover public service schemes by [Schedule 4 of the Public Service Pensions Act 2013](#).
200. Section 70 imposes the duty to report on a number of individuals including a member of the pension board of a public service scheme and a professional adviser to such a scheme. The term professional adviser is defined in [section 47 the Pension Act 1995](#) and includes the auditor appointed by the trustees. Although section 47 refers specifically to occupational pension schemes, and auditors in the public sector are not appointed by the trustees, the TSU has confirmed with the Pension Regulator that they expect the duty to nevertheless apply to auditors of public service pension schemes.
201. Auditors are therefore required to provide a written report to the Pension Regulator from April 2015 if they have reasonable cause to believe that a legal duty relevant to the administration of the scheme has not been complied with, and that failure is likely to be of material significance to the regulator. Auditors should contact the TSU for advice if such a situation arises in practice.

## Corporate governance developments

### New code on fraud and corruption

202. CIPFA has issued a code of practice and guidance notes to provide the basis for counter fraud arrangements across the public sector. The *Code of practice on managing the risk of fraud and corruption* consists of the following five groups of principles that set out a body's responsibilities for establishing good counter fraud practice and the form that will take
- The governing body should acknowledge its responsibility for ensuring that the risks associated with fraud and corruption are managed effectively across all parts of the organisation.
  - Fraud risk identification is essential to understand specific exposures to risk, changing patterns in fraud and corruption threats and the potential consequences to the organisation and its service users.
  - An organisation needs a counter fraud strategy setting out its approach to managing its risks and defining responsibilities for action.
  - The organisation should make arrangements for appropriate resources to support the counter fraud strategy.

- The organisation should put in place policies and procedures to support the counter fraud and corruption strategy and take action to prevent, detect and investigate fraud.

203. The guidance notes consider the implementation of the code and share examples of good practice. This includes interpretations to highlight where sectoral differences should be taken into account.

## Auditor action checklist

		Yes/No/N/A	Initials/date	W/P ref
1	Have you read the management commentary in accordance with the guidance at paragraph 196?			
2	Have you carried out the action recommended at paragraph 198 in respect of holiday pay?			
3	Have you carried out the action required at paragraph 201 in respect of reporting to the Pension Regulator?			

## TSU contact for cross-sector chapter

204. The contact in the TSU for this chapter is Paul O'Brien, Senior Manager (Technical) - 0131 625 1795 or [pobrien@audit-scotland.gov.uk](mailto:pobrien@audit-scotland.gov.uk).

# Technical Services Unit

Audit Scotland's Technical Services Unit (TSU) informs the professional judgement of appointed external auditors on technical matters and encourages the proper exercise of professional scepticism to improve the quality of the audit delivered to the Accounts Commission and Auditor General for Scotland. The TSU provides authoritative guidance and practical assistance to support appointed auditors in carrying out their responsibilities under the *Code of audit practice* to

- provide an opinion on audited bodies' financial statements and, where required, the regularity of transactions
- review and report on other information published with the financial statements, including governance statements and remuneration reports
- examine and report on approved grant claims and other returns submitted by local authorities
- review and report on whole of government accounts returns.

Contact details for relevant TSU staff are included at the end of each chapter.

**Feedback on technical bulletins is encouraged and should be sent to**

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